

AMENDED IN ASSEMBLY MARCH 14, 2011

CALIFORNIA LEGISLATURE—2011–12 REGULAR SESSION

ASSEMBLY BILL

No. 229

Introduced by Assembly Member Lara

February 2, 2011

An act to amend Section 12410.5 of, to add Sections 12410.6, 12410.7, and 12410.9 to, and to add and repeal Section 12410.8 of, the Government Code, relating to audits.

LEGISLATIVE COUNSEL'S DIGEST

AB 229, as amended, Lara. The Controller: audits.

Existing law requires the Controller to superintend the fiscal concerns of the state. Existing law requires the Controller to receive every audit report prepared by any local ~~public~~ agency *to comply with the federal Single Audit Act of 1984*.

This bill would require the *audit reports prepared in this regard to be submitted to the Controller to receive every annual financial audit report prepared by any local government within 9 months of the end of the audit period audited or within a longer timeframe authorized by the Controller in accordance with applicable federal law. This bill would authorize the Controller to appoint a qualified certified public accountant to complete an audit report if it is not submitted by the local agency within the required timeframe, with associated costs to be borne by the local agency, as specified.* This bill would require ~~an~~ the audit conducted pursuant to this provision to ~~fully~~ comply fully with the Government Auditing Standards issued by the Comptroller General of the United States. This bill would require the audits to be made by a certified public accountant that is licensed by the California Board of Accountancy and selected by a local ~~government~~ agency *from a*

directory of accountants to be published by the Controller by December 31 of each year. The Controller would be required to use specified criteria to determine those certified public accountants that are to be included in the directory.

This bill would require the Controller to develop a plan to review and report the financial and compliance audits of ~~cities, counties, and special districts~~ local agencies. This bill would require the Controller, in consultation with specified entities, to propose and adopt the content of an audit guide. This bill would also require the Controller to report to the Legislature by January 31 of each year the results of ~~its~~ the controller's oversight activity. The requirement that the Controller report to the Legislature would be repealed on December 31, 2015.

Vote: majority. Appropriation: no. Fiscal committee: yes.
State-mandated local program: no.

The people of the State of California do enact as follows:

1 *SECTION 1. The Legislature finds that financial audits provide*
2 *an independent assessment of, and reasonable assurance about,*
3 *whether local agencies' reported financial condition, results, and*
4 *use of resources are presented fairly in accordance with recognized*
5 *standards. Accordingly, it is the intent of the Legislature to promote*
6 *accountability over local government funding by establishing a*
7 *process for reviewing and reporting on financial and compliance*
8 *audits conducted of local agencies. It is further the intent of the*
9 *Legislature that the Controller shall have oversight responsibilities*
10 *for implementing and ensuring compliance with this act.*

11 ~~SECTION 1.~~

12 *SEC. 2. Section 12410.5 of the Government Code is amended*
13 *to read:*

14 12410.5. (a) The Controller shall receive every annual financial
15 audit report prepared for any local ~~government~~ agency, *as defined*
16 *in Section 53980*, including those reports prepared in compliance
17 with the federal Single Audit Act of 1984 (P.L. 98-502; 31 U.S.C.
18 Sec. 7501 et seq.) and required under any law to be submitted to
19 any state agency, and shall, after ascertaining its compliance with
20 that federal act, transmit the report to the designated state agency.

21 ~~(b) It is the intent of the Legislature to promote accountability~~
22 ~~over local government funding by establishing a new program to~~
23 ~~review and report on financial and compliance audits of cities,~~

1 counties, and special districts. It is further the intent of the
2 Legislature that the Controller shall have the primary responsibility
3 for implementing and overseeing the program. Financial audits
4 provide an independent assessment of, and reasonable assurance
5 about, whether an entity's reported financial condition, results,
6 and use of resources are presented fairly in accordance with
7 recognized criteria. Reporting on financial audits that are performed
8 in accordance with government auditing standards also includes
9 reports on internal control, compliance with laws and regulations,
10 and provisions of contracts and grant agreements as they relate to
11 financial transactions, systems, and processes. Compliance audits
12 shall be defined in generally accepted auditing standards as a
13 program-specific audit or an organization-wide audit or an entity's
14 compliance with applicable compliance requirements. Financial
15 and compliance audits conducted under this chapter shall fulfill
16 federal single audit requirements.

17 (e)

18 (b) An audit ~~conducted~~ for any local agency submitted to the
19 Controller pursuant to this section shall comply fully with the
20 Government Auditing Standards issued by the Comptroller General
21 of the United States.

22 (d) ~~The audits~~

23 (c) An audit for any local agency submitted to the Controller
24 pursuant to this section shall be made by a certified public
25 accountant, licensed by the California Board of Accountancy, and
26 selected by the local ~~government~~ agency, as applicable, from a
27 directory of certified public accountants deemed by the Controller
28 as qualified to conduct audits of local ~~governments~~ agencies which
29 shall be published by the Controller not later than December 31
30 of each year. The certified public accountant shall possess
31 individual education, examination, and experience qualifications
32 that have been determined by the board to be substantially
33 equivalent to the qualifications under Section 5093 of the Business
34 and Professions Code, and that are in accordance with subdivision
35 (b) of Section 27 ~~of Article 4 of Division 1~~ of Title 16 of the
36 California Code of Regulations necessary to perform the full range
37 of accounting services, including signing attest reports on attest
38 engagements.

1 (1) In determining that certified public accountants shall be
2 included in the directory, the Controller shall use the following
3 criteria:

4 (A) *The certified public accountants or public accountants shall*
5 *be in good standing as certified by the California Board of*
6 *Accountancy.*

7 ~~(A)~~

8 (B) The certified public accountants or public accountants, as
9 a result of a quality control review conducted by the Controller
10 pursuant to Section 12410.9, shall not have been found to have
11 conducted an audit in a manner constituting noncompliance with
12 subdivision (c) of that section.

13 ~~(B) The certified public accountants or public accountants shall~~
14 ~~be in good standing as certified by the Board of Accountancy.~~

15 (2) It is the intent of the Legislature to ensure that auditors and
16 audit organizations maintain their independence in appearance and
17 in fact by rotation of public accounting firms. Beginning with the
18 2011–12 fiscal year, a local government agency shall be prohibited
19 from using the same public accounting firm to perform an annual
20 financial and compliance audit for more than five consecutive
21 years. The Controller may waive this requirement if he or she finds
22 that no qualified auditor is otherwise available to perform the audit.

23 ~~(e)~~

24 ~~(d) The governing board of each city, county, and special district~~
25 ~~local agency shall include all of the following in their its contracts~~
26 ~~for audits:~~

27 (1) A provision to withhold 10 percent of the audit fee until the
28 Controller certifies that the audit report conforms to the reporting
29 provisions of subdivision (a) of Section 12410.7.

30 (2) A provision to withhold 50 percent of the audit fee for any
31 subsequent year of a multiyear contract if the prior year's audit
32 report was not certified as conforming to the reporting provisions
33 of subdivision (a) of Section 12410.7. This provision shall include
34 a statement that a multiyear contract shall be null and void if a
35 public accounting firm or independent auditor is declared ineligible
36 pursuant to subdivision (d) of Section 12410.9. The amount
37 withheld shall not be payable unless payment is ordered by the
38 board or the audit report for that subsequent year is certified by
39 the Controller as conforming to the reporting provisions of
40 subdivision (a) of Section 12410.7.

1 (3) A provision that will provide the Controller access to audit
2 working papers.

3 ~~SEC. 2.~~

4 *SEC. 3.* Section 12410.6 is added to the Government Code, to
5 read:

6 12410.6. (a) The Controller shall develop a plan to review and
7 report on financial and compliance audits of ~~cities, counties, and~~
8 ~~special districts~~ *local agencies*. The Controller, in consultation
9 with the Department of Finance, ~~the Legislative Analyst's Office,~~
10 ~~state agencies,~~ and representatives of the League of California
11 Cities, the California State Association of County Auditors, and
12 the California Society of Certified Public Accountants, shall
13 propose the content of *and adopt* an audit guide.

14 (b) The audit reports shall be submitted to the Controller ~~in~~
15 ~~accordance with Public Law 104-156~~ within nine months after the
16 end of the period audited, ~~or within a longer timeframe authorized~~
17 ~~by the Controller.~~ *in accordance with applicable federal law.*

18 (c) If the audit reports required by ~~subdivision (b) of~~ Section
19 12410.5 have not been ~~filed by a local government with the~~
20 ~~Controller's office on or before the due date established under~~
21 ~~subdivision (b), the Controller's office shall determine the most~~
22 ~~advantageous method of obtaining the required audited financial~~
23 ~~statements.~~ *submitted by a local agency to the Controller on or*
24 *before the due date established by this section, the Controller shall*
25 *appoint a qualified certified public accountant to complete the*
26 *report and to obtain the information required. Any cost incurred*
27 *by the Controller pursuant to this subdivision, including contracts*
28 *with, or the employment of, the certified public accountants in*
29 *compiling the audit report shall be borne by the local agency and*
30 *shall be a charge against any unencumbered funds of the local*
31 *agency.*

32 ~~SEC. 3.~~

33 *SEC. 4.* Section 12410.7 is added to the Government Code, to
34 read:

35 12410.7. (a) To determine the practicability and effectiveness
36 of the audits and audit guide, the Controller on an annual basis
37 shall review and monitor the audit reports performed by
38 independent auditors. The Controller shall determine whether the
39 audit reports conform with the reporting provisions of subdivision
40 (b) of Section 12410.9 and shall notify each ~~local government~~

1 agency, and the auditor of each local ~~government~~ agency regarding
2 each determination.

3 (b) The independent auditor shall correct his or her audit report
4 within 30 days of notification of any deficiency. The Controller
5 may suspend the independent auditor from performing any local
6 ~~government~~ agency audits if the auditor does not correct his or her
7 audit report within 30 days of the Controller's notification.

8 ~~SEC. 4.~~

9 *SEC. 5.* Section 12410.8 is added to the Government Code, to
10 read:

11 12410.8. (a) The Controller shall report to the Legislature by
12 January 31 of each year the results of ~~its~~ *the Controller's* oversight
13 activity, including the results of ~~its~~ *the Controller's* quality control
14 reviews.

15 (b) A report submitted pursuant to subdivision (a) shall be
16 submitted in compliance with Section 9795.

17 (c) Pursuant to Section 10231.5, this section is repealed on
18 December 31, 2015.

19 ~~SEC. 5.~~

20 *SEC. 6.* Section 12410.9 is added to the Government Code, to
21 read:

22 12410.9. (a) The Controller may perform quality control
23 reviews of audit working papers to determine whether audits are
24 performed in conformity with government audit standards and the
25 local ~~government~~ agency audit guide. The Controller shall
26 communicate the results of his or her reviews to the Department
27 of Finance, the independent auditor, and the local ~~government~~
28 agency for which the audit was performed, and shall review his
29 or her findings with the independent auditor.

30 (b) Prior to the performance of any quality control reviews, the
31 Controller shall develop and publish guidelines and standards for
32 those reviews. Pursuant to the development of those guidelines
33 and standards for those reviews, the Controller shall provide an
34 opportunity for public comment. The Controller shall update the
35 guidelines and standards for any changes in audit standards.

36 (c) The Controller is responsible for selecting audits for review
37 based on criteria, including, but not limited to, disciplinary actions
38 by the California Board of Accountancy, results of the Controller's
39 review and monitoring of the audit reports, the extent of findings
40 in the audit reports issued by the independent auditor, the number

1 of audits of local ~~government~~ *agencies* performed annually by the
2 independent auditor, the independent auditor's experience in
3 performing audits of local ~~governments~~ *agencies*, the complexity
4 of state and federal programs administered by the local ~~government~~
5 *agencies*, and requests or leads from other sources.

6 (d) If the quality control review of the Controller indicates that
7 the audit was conducted in a manner that may constitute
8 unprofessional conduct as defined pursuant to Section 5100 of the
9 Business and Professions Code, including, but not limited to,
10 breach of fiduciary responsibility of any kind, gross negligence,
11 repeated negligent acts resulting in a material misstatement in the
12 audit or failure to disclose noncompliant acts, the Controller shall
13 refer the case to the California Board of Accountancy. If the
14 California Board of Accountancy finds that the independent auditor
15 conducted an audit in an unprofessional manner, the Controller
16 may prohibit the independent auditor from performing any audit
17 of a local ~~government~~ *agency* for a period of three years, in addition
18 to any other penalties that the California Board of Accountancy
19 may impose. In any matter that is referred to the California Board
20 of Accountancy, the Controller may suspend the independent
21 auditor from performing any local ~~government~~ *agency* audit
22 pending final disposition of the matter by notice and an opportunity
23 to respond to that suspension. The independent auditor shall be
24 given credit for any period of suspension if the California Board
25 of Accountancy prohibits the independent auditor from performing
26 audits of the local ~~education~~ *agency* under subdivision (c). In any
27 event, the Controller shall not suspend an independent auditor
28 under this subdivision for a period of more than three years.